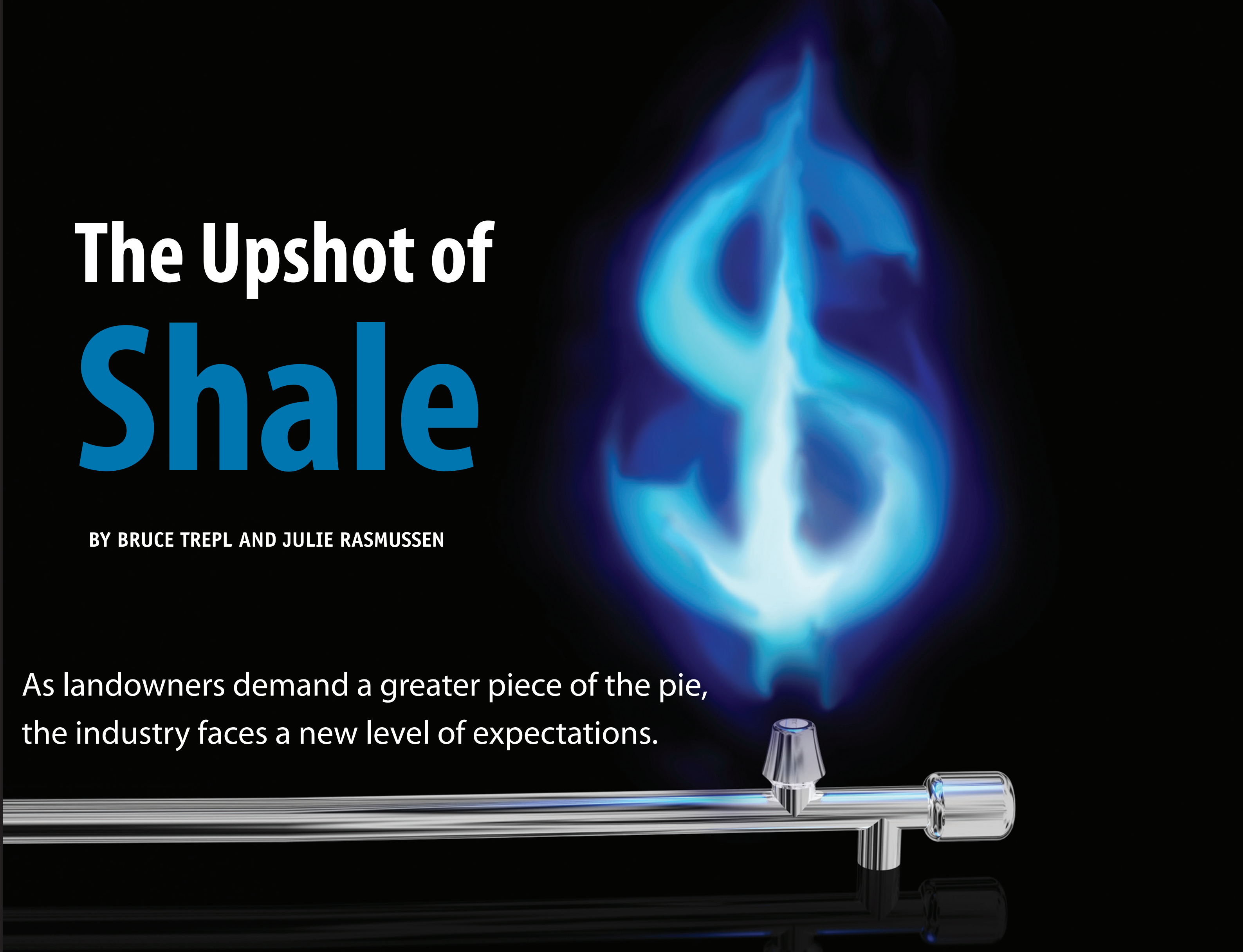


The Upshot of Shale

BY BRUCE TREPL AND JULIE RASMUSSEN

As landowners demand a greater piece of the pie, the industry faces a new level of expectations.

The breakthrough in natural gas supply in North America has been a real game-changer. According to the Interstate National Gas Association of America (INGAA), natural gas currently provides about 25 percent of the daily energy that is consumed in the United States. A recent INGAA study projects that natural gas use in North America will grow by 18 percent by 2030 and, depending on energy markets and public policies, could grow by as much as 34 percent. The 2012 Annual Energy Outlook published by the U.S. Energy Information Administration reports that shale gas production is expected to triple by 2035.

In terms of domestic supply, the Bakken, Marcellus, Eagle Ford, Haynesville and Barnett shale plays have received most of the attention, but they are only the tip of the iceberg. All of this increased natural gas production has necessitated new pipeline development and existing pipeline upgrades.

Underground Construction and Pipeline & Gas Journal's 2012 worldwide pipeline survey figures indicate that 118,623 miles of pipelines are currently planned and/or under construction. Of these, 88,976 represent projects in the planning and design phase; 29,647 miles reflect pipelines in various stages of construction. Almost 32,000 miles of pipeline are currently being planned for North America.

Increased natural gas and shale pipeline development has triggered significant growth in, and attention on, the right of way industry. In response, right of way professionals must be prepared to deal with the issues that have resulted, such as staffing costs, increasing land values, landowner expectations and eminent domain.

Escalating Landowner Expectations

The U.S. and Canada are now sitting on one of the biggest energy booms ever. Thanks to improved hydraulic fracturing and new advances in drilling techniques, shale formations have become hotbeds of North American drilling activity. This is due to technological advances that have made it possible to extract the plethora of fossil fuels trapped between the rocks. With billions of dollars worth of revenue at stake, the land surrounding these shale hotbeds have experienced a land grab similar to the California Gold Rush of the 1800s. Prices for rights of way are escalating, and landowners are ready to claim their share of this newfound wealth.

Not too long ago, a right of way agent could negotiate $50 a rod (16.5 feet), basing their offer on current land values in some areas. Today, a rod can go for as high as $500. This price increase is a result of energy companies willing to pay higher rates in an attempt to keep their project on time and moving quickly to production. One might claim that this is placing too much value on the land, but the reality is that landowners have become more knowledgeable about what energy companies are willing to pay to meet their deadlines. This competitive landscape has pushed up land values significantly. Data compiled by Thomson Reuters showed that over $473 billion in energy asset transactions were completed in 2011. Landowners want their piece of the pie and have become more adept at negotiations as a result.

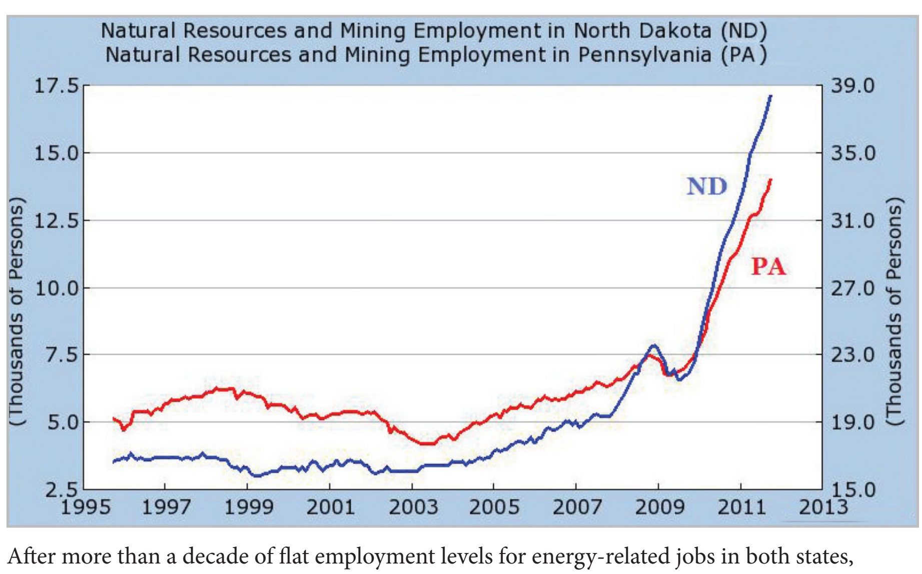
Landowners will often use environmental concerns as a negotiation tactic. Environmental issues can quickly become publicized even if the concerns are unfounded. Our experience shows that when faced with opposition from a true environmental organization, the best defense is a good offense. This means taking steps necessary to ensure the proper message is getting out to the public. Very often, opposition stems from misinformation and poor communication between project representatives and the community.

The longer a shale area has been worked, the savvier the typical landowner becomes. Companies find themselves making concessions regarding terms of the original agreement in order to finalize negotiations quickly. When a well is near completion, neither the producer nor the pipeline company can expect a revenue stream until the well head is tied in and the product is flowing. This translates to simple economics.

The Domino Effect

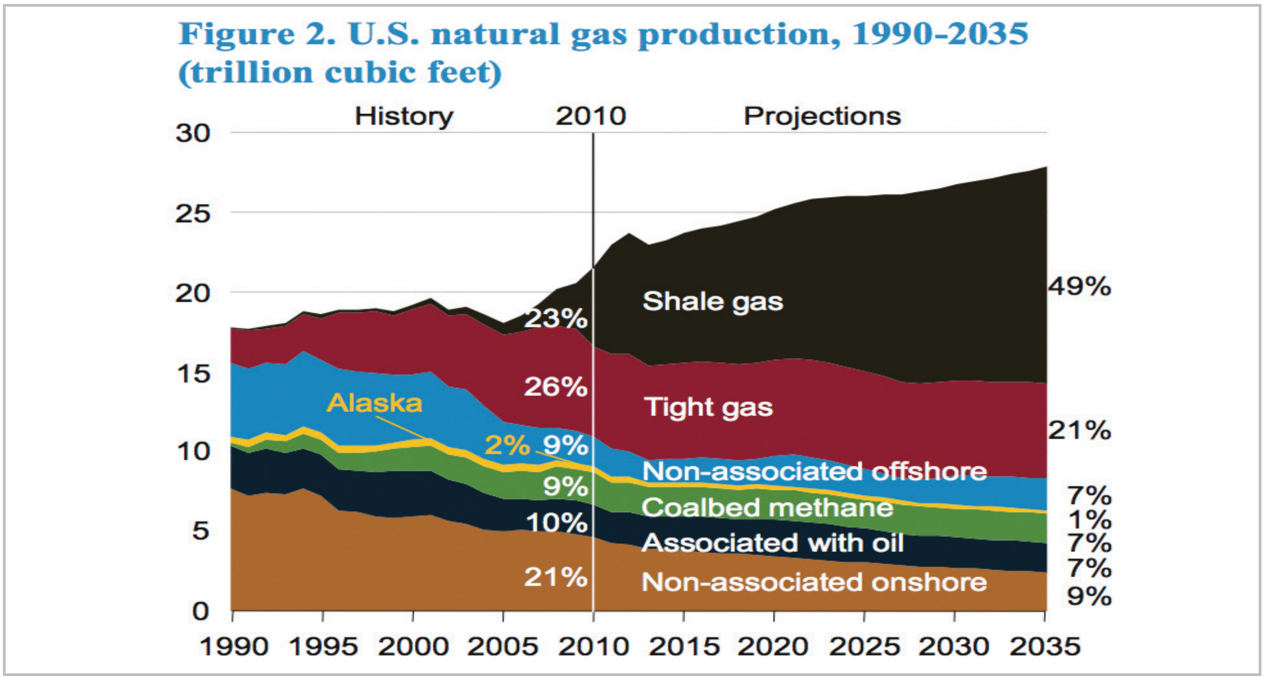
A last minute project change can cause a chain reaction of issues that need to be resolved before the pipeline can start producing. Any type of delay equates to lost revenue for the company. Therefore, paying additional compensation to a holdout landowner or agreeing to extreme terms may be the only viable option to get the product flowing. However, this strategy typically leads to increased costs for future projects. The compensation provided to the holdout has now become the standard and will be expected in the next negotiation. If that same landowner is given another opportunity to benefit financially, their expectations and your appraised land value may be thousands of dollars apart.

In most cases, companies will pay the going rate in a particular area regardless of how that rate was determined. Companies need to get their project completed, which means they are often at the mercy of the landowner when it comes to determining the value of their land. A skilled negotiator is clearly required to navigate this system, as there is no set process used in acquiring land. Companies and consultants agree that a consistent acquisition process would be helpful, but at this time, such a process does not exist outside of what a skilled negotiator is able to implement.



After more than a decade of flat employment levels for energy-related jobs in both states, employment levels have been booming, along with the Bakken oil boom in North Dakota and the Marcellus natural gas boom in Pennsylvania. Source: U.S. Bureau of Labor Statistics.

2012 Annual Energy Outlook



According to the U.S. Energy Information Administration's Annual Energy Outlook 2012 Early Release Overview, shale production is projected to increase from 23% of total natural gas production to 49% by the year 2035.

Eminent Domain

Eminent domain continues to be a hot topic in shale regions. If you are currently working in a shale region, you have probably heard a great deal of talk about new legislation protecting the rights of communities and landowners. For example, the Texas State Legislature has enacted Senate Bill 18, a law that substantially changes eminent domain practices for both public and private entities. The new rule will make condemnations more time-consuming and costly.

With this change, acquisition schedules need to be adjusted in the event that voluntary agreements cannot be reached. Because of this, companies are focused on finding routing alternatives in an attempt to avoid these situations. Of course, this takes time and money, and in areas where landowners have titles to large land holdings, routing alternatives may not always be possible.

When time and resources permit, companies can file a condemnation action. In some regions, awards are coming back grossly inflated and do not reflect the true value for the rights being sought. When this happens, many companies are not accepting the egregious awards and are appealing these rulings to a higher court. This represents an attempt to enforce the true value of an easement and damages.

If the timelines are compressed and eminent domain does not apply to the project, pipeline routing becomes the main focus. A review of impacted and adjacent land along the preferred routing should be evaluated. When a major landowner is being largely impacted by a project, early consultations should be made with that landowner to obtain preliminary support of the routing. Landowners are becoming much more skilled in their negotiations than ever before. Therefore, before the survey process, it is essential that an option to protect the proposed routing has been secured.

In the past, landowners that granted access to perform surveys would generally not oppose the project. However, the current situation has changed. Landowners have been coached by attorneys to allow the initial survey. Knowing that the company has already spent significant dollars to perform environmental and civil surveys and map the best route for the project, landowners feel they are in a much better position to negotiate for a higher compensation.

Landowners are aware that companies may relent to their demands as a result of schedule constraints and additional expenses that a routing change would incur. In response, agreements should be drafted to allow companies flexibility in the final placement of the pipeline. Whenever possible, placement options should be secured instead of, or along with, the traditional survey permission. While there is a cost associated in securing options, these options are worth the security by ensuring that time and money is not lost in late-in-the-game routing changes.

Staffing Costs

As shale regions explode with volumes of personnel, communities benefit financially from this growth in population. Hotels fill up rapidly, RV parks are at capacity and vacant apartments have become a thing of the past. Restaurants are packed, and stores cannot keep supplies on their shelves. Help wanted signs litter the landscape of areas in North Dakota and Pennsylvania, where fast food chains advertise starting wages at over $15 an hour to potential employees.

For right of way agents, this has an enormous impact on the cost of living. A right of way agent is expected to live off the General Services Administration (GSA) Continental United States (CONUS) per diem rate set by the government. The current GSA CONUS per diem rate will not cover the cost of a hotel room in most shale areas, let alone meals. While the GSA rates are modified in October of each year, they still do not reflect the true cost of living in shale regions due to the explosion of housing demand. It is not unheard of for a right of way professional to spend a night in his car, turn his car into a "vehicle suite," to bunk with several other agents, or to travel out of the area to find a bed to sleep in.

Many energy companies recognize that it is difficult to convince experienced agents to work in the field when the per diem does not cover their actual cost of living. As a result, they are starting to offer alternative solutions to the GSA per diem rate, such as covering actual expenses, increasing the per diem rate or providing living accommodations in company built "man-camps," which may offer services such as meals and laundry services.

Recognizing that there is an abundance of opportunities for agents to select for whom and where they want to work, companies are focused on attracting and retaining top performing agents in shale regions. Employers want to retain and reward agents who have expert negotiation skills, as prolonged negotiations are costly and companies do not want project timelines to be compromised. As a result, more and more companies are offering incentives such as bonuses for work that is completed on time or ahead of schedule and five-day work weeks, which make it easier for right of way agents to be with their families on the weekends.

Energy Independence

The probable natural gas deposits in the United States are estimated at roughly sixty years of the current annual U.S. demand, and domestic shale gas production is projected to increase from 23% share of total natural gas production to 49% by the year 2035. As we continue to improve the industry technology and leverage the vast potential of natural gas deposits available, we are well on our way to energy independence.

The natural gas pipeline industry is poised for takeoff, and right of way professionals have the knowledge, expertise and integrity necessary to facilitate this growth. As the energy industry becomes more focused on the production of natural gas, opportunities for the right of way industry will continue to flourish. The industry looks forward to what the future of shale holds, and over the coming decades, we will continue to see profound developments. This is an exciting time, and we can all look forward to the challenges and opportunities that will surely follow.

References

Interstate Natural Gas Association of America

People v Ocean Shore R.R. (1948) 32 C2d 406, 424, 196 P2d 570.

People ex rel Dep't of Pub. Works v TeVelde (1970) 13 CA3d 450, 91 CR 556.

Shale Gas and New Petrochemicals Investment: Benefits for the Economy, Jobs and U.S. Manufacturing – American Chemistry Council, March 2011

U.S. Energy Information Administration, Annual Energy Outlook 2012

www.naturalgas.org

Bruce Trepl

Bruce is Project Director at Contract Land Staff, LLC, and has more than 10 years of industry experience, including pipeline, oil and gas, water lines and due diligence. He currently oversees pipeline projects in Oklahoma, Kansas and Colorado, working with clients in project planning, estimating, budgeting, resource allocation and quality control. Bruce holds a BA from West Texas A&M University and serves as an instructor for the CLS Professional Development Institute.

Julie Rasmussen

As Senior Vice President of Projects and Operations at Contract Land Staff, LLC, Julie has 18 years of experience in land management and right of way project oversight. She has managed large multi-state pipeline projects, overseeing regulatory compliance with federal agencies, route selection, acquisition, scheduling, damage settlements, permitting, feasibility studies and budgeting. Julie is a licensed North Carolina Real Estate Broker and an instructor for the CLS Professional Development Institute.